A PROMISING VENTURE IN INDUSTRIAL PARTNERSHIP

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Though not yet tested by years of experience, the industrial partnership scheme of the Dennison Manufacturing Company, of Massachusetts, bears the marks of successful coping with baffling industrial problems. It is not a measure to purchase peace merely. It is not in any usual sense a measure to promote efficiency. Nor does it offer a substitute for normal wages. It aims, first of all, to secure the permanency of a successful business, and it employs to this end a method which, for the time and in the long run, should make for both peace and efficiency. It has distinct limitations, accepted from the desire to avoid defects everywhere arising in profit-sharing plans. But it will be regarded as unphilanthropic only by persons who do not hold that good industrial management prolonged over indefinite years is genuinely philanthropic.

In the first instance the problem which the Dennison Company is trying to solve is a business man's and investor's problem. And it is surely a universal problem. It arises in a new and resourceful country like the United States quite as inevitably as in old countries. Its essentials are clearly and simply stated by Marshall: "It would therefore at first sight seem likely," he says, "that business men should constitute a sort of caste, . . . founding hereditary dynasties, which should rule certain branches of trade for many generations together. But the actual state of things is very different. For when a man has got together a great business, his descendants often fail, in spite of their great advantages, to develop the high abilities and the special turn of mind and temperament required for carrying it on with equal success. . . . For a time indeed all may go well. . . . But when a full generation has passed, when the old traditions are no longer a safe guide, and when the bonds that held together the old staff have been dissolved, then the business almost invariably falls to pieces unless it is practically handed

over to the management of new men who have meanwhile risen to partnership in the firm. . . . But in most cases his descendants arrive at this result by a shorter route. . . . They sell the business to private persons or a joint-stock company; or they become sleeping partners in it; . . . in either case the active control over their capital falls chiefly into the hands of new men."[1]

For the good of the workmen and their employers and for the good of the purchasing community, it is desirable that the "new men" who continue a business should be experienced, successful and active managers. Whence will they come? Industrial history is strewn with cases in which the whole body of workmen have been admitted to joint management; but so rarely have they been successful that their chroniclers find it necessary to invoke special explanations of success, and generally it is easier, with Marshall, to explain failure. The development of the last half century has been different: shareholders in corporations have become the managers of industry. Those who praise most the limited liability organization of industry, resting upon the issue of shares that are sold on the stock exchanges, do not deny that tangible imperfections exist in this modern system. A magnificent opportunity to attract capital from every corner of the land has been developed, and great mobility of capital has followed. But the evil of irresponsible absentee ownership is only beginning to be appreciated. The stock exchanges are a happy hunting-ground for persons whose first interest it is to secure control of corporations, to play with accounts so as to publish large earnings or grievous deficits, to boost dividends and stock prices, and in due time to let confiding "widows and orphans" elect directors. Even when such procedures, and they are legal enough, do not occur, it remains true that most stockholders know little of their business and vote blindly. Not often is it much to their credit if the corporation prospers and pays large dividends.

Meanwhile the employees of the corporation, high and low, can do nothing to prevent destructive management by outsiders. And their extra efforts and care may redound to the advantage of professional gamblers, mere lucky or shrewd inactive purchasers of stock or the passive heirs of the deceased founder. Small wonder if workmen fail to vaunt the dignity of labor and hesitate to do their best.

Somewhere within the ranks of the employees of a great company

[1] Marshall, *Principles of Economics*, pp. 379-380.

are surely to be found most of the men who, as the world goes to-day, are best schooled and qualified to run it. The tests of their fitness, the tests of the fitness of all men in the company, are not tests that outsiders can with unerring sureness apply. And if in truth management is a function exercised not merely by one man or a board of directors with reference to the whole company, but by many men and at countless points, with reference to the divisions and departments within the company, then it may be a measure of justice to distribute some part of the rewards of management to all the managers. Such an application of justice may at the same time insure excellence of management. Let us see who these managers, not generally so classified, are.

At some point in the scale of remuneration of every large company occurs a natural division of the workers into two groups. Below the point are those workers whose labor is mainly of a routine character. By special care or effort they can save from their own time or energy or material. They can turn out the same product in fewer hours, or with less effort, or with less waste of materials or power. The problem of their remuneration is essentially one of paying wages in proportion to output, and that problem is perhaps best met at present by some safeguarded variety of piece wage.

Above this group are those workmen who can exercise imagination, often enough men promoted for their fitness from the lower group. They have initiative, they originate. They are men who can think calmly and clearly of two things at once. They can by mechanical rearrangement secure real economies, economies independent of extra strain by workmen. They can exercise discretion in buying materials or selling finished product, and by their understanding of a complicated situation may exercise their discretion wisely and profitably. For their success they are further promoted in position or salary. From the most successful of them the higher officers and the directors of the company are naturally chosen. Since increased profits of the company are so intimately dependent on the energies of the entire active managing body, and not on stockholders who send proxies or have an otherwise external relation, should not the entire increase of profits of the company go to these men? That they should, and that thereby the finest *morale* of the company may be preserved and indefinitely continued, has been the belief of the re-incorporators of the Dennison Company.

The stockholders of the old company became under the new the owners of first preferred stock to the amount of $4,500,000, on which a cumulative dividend at the rate of eight per cent is due. Provision is made for the issue of second preferred stock in series, each series having an unchangeable rate of dividend not less than four per cent. The circumstances of the issue of this stock are stated below. After dividends on the first and second preferred stocks have been paid, there will be deducted annually from the remaining net profits five per cent of the remainder for the purpose of buying in shares of first preferred stock upon favorable occasion.

An issue of industrial partnership stock to the amount of $1,050,000 is authorized. Such stock may be owned only by so-called principal employees, the group already described. They are persons who in the previous year have received for their labors (*a*) $1,200 or over and been seven years in service; (*b*) $1,500 and six years in service; (*c*) $1,800 and five years. Such principal employees receive shares of industrial partnership stock in a number proportional to their wages. Stock shall not be issued for cash, but shall represent profits of the company, and therefore be distributed without special charge to those whose peculiar efforts are chiefly, in the long run, the means of securing the profits. But no new issue of industrial partnership stock shall take place until a five per cent cash dividend has been paid on the outstanding industrial partnership stock. To insure the frequent, probably annual, issue of such stock, no cash dividend upon it shall ever exceed twenty per cent in one year.

A crucial question in this connection is, how shall the issues of industrial partnership stock be apportioned? Certainly by no human device can the final profits of a complex business be perfectly ascribed to individual workmen composing the business. Yet a working approximation seems not impossible. In the salaries that men get there is a kind of index to their comparative values to the business; no perfect index again, yet one that results from the best available discernment. Let him whose salary is twice that of another, receive twice the other's allotment of stock. Industrial partnership stock is issued in $10 denominations, so that many gradations of amount may be adequately expressed.

Where ordinary remuneration is the basis of issues of new stock, there appears an incentive for each man to make himself worth more in the daily execution of his tasks and so to qualify himself for another

position which would bring not only a higher salary, but, correspondingly, a more liberal allotment of stock.

Only active workmen still in service may be holders of industrial partnership stock. That is partly because of arrangements as to voting, presently to be described, but chiefly in order that future increments of profit may be divided only among those who may be regarded as responsible for them . Hence in case an employee leaves the company or dies, his stock may either be purchased by the company for cash or converted by the company into second preferred stock paying an unvarying rate of dividend and never receiving an allotment of new stock. So the retiring employee may receive and, as the case may be, may bequeath to others a capital amount representing his saved earnings, but he may not transmit a claim to increased future profits which he and his descendants have not helped to create. At the option of the company cash may be paid, instead of second preferred stock, to the retiring owner of industrial partnership stock.

What this arrangement implies when read in the light of the position and destiny of the preferred stocks is the most interesting part of the Dennison scheme. In all probability a considerable amount of industrial partnership stock will be issued, but it may be some years before $1,000,000 will be outstanding. Until that date arrives, stockholders of all classes will vote according to the capital value of their shares, the holder of one share of first preferred stock, par $100, and the holder of ten shares of industrial partnership stock, par $10, will each have in so far one vote. The larger the amount of industrial partnership stock, the safer will be the return on the preferred stocks. When $1,000,000 of industrial partnership stock is outstanding, the preferred stocks will have sufficient safety no longer to require a vote. Then their holders will cease to vote and the entire management of the concern will fall to the principal employees. These are the persons most fit to manage, the persons who have risen from the lower places, the persons qualified by proved ability and experience to manage the business. Hitherto they have been merely employees, and though performing some of the functions of managers, have not had corresponding authority and privileges in the conduct of the business. Henceforth, as part owners of the business, with an income, above wages, that is large or small according to the character of their management, they will have enough at stake

to be trusted as sole managers. Should they fail in their task, reducing, and then maintaining for some time, the dividends of the preferred stocks below the stipulated rates, then the preferred stockholders may resume the management, to retain it until the rates are restored. But for an extended period of inability to pay preferred dividends, such a period as proves that the assets behind the industrial partnership stock have disappeared, the first preferred stockholders shall take over and permanently retain the voting power.

Such collapse seems unlikely. Provisions for redeeming in cash the stock of persons leaving the business, and for buying in shares of the first preferred stock, should prevent the burden of fixed dividend charges from becoming excessive. Also, the checks upon the dividend rate of the industrial partnership stock should lead to a large increase in the outstanding amount of this more variable security. Having lost their vote, the preferred stockholders would become akin to bond creditors. The business would more and more approach the form of a pure industrial partnership. The guarantee of its efficiency and permanence as an industrial partnership would depend, negatively, on continuing to exclude from the profits of management those persons receiving less than $1,200 and only recently taken into employment, and on excluding them from voting. But quite as much the guarantee of success would depend, positively, on assigning new stock according to salary and allowing the vote according to shares of stock held.

By this arrangement the central causes of previous failures are eliminated. There is danger of failure when low-paid workmen are admitted to the profits of management, chiefly because they are not true managers, and perhaps because they would be receiving the gains of others and so disaffecting the others. There is danger of failure when employees only a short time in engagement with the company are given a share in profits and a vote. There is danger of failure under outright welfare arrangements and provision for postponed rewards. There is danger of failure when, as in producers' cooperative systems, each man gets only one vote, no matter what his position with the company; then jealousy of the managers, desire to reduce their salaries, even deposition of the managers, may break down efficiency.[2]

[2] For a brief statement of the usual weaknesses of profit-sharing schemes see Taussig's *Principles of Economics*, vol. II, pp. 303 *ff*. See also Schloss' *Methods of Industrial Remuneration*. The rapidly expanding literature on efficiency in business contains in detail much that is pertinent.

Along with the internal safeguards described, the external safeguard is perfectly exemplified. The speculative stockholder, the ignorant and indifferent stockholder, the scheming broker, all these are excluded from the management, when at his best the absentee stockholder, acting through his representatives, the directors, only manages the business by selecting and promoting the able workmen within it. In the Dennison Company, as in many others, the directors themselves have commonly if not always risen from the ranks. The more democratic the business, the more this is likely to be the case; and the less will the employer seem to be the exploiter. Some persons are sceptical of democratic tendencies in business, but even such should discern the essential promising features of the present experiment: first, that the death of the founder does not tend to the disintegration of the business; second, that the workmen may feel that, though they do not wholly own their business, yet their extra productive effort, their co-operative loyalty in expending effort, will return extra profit to themselves alone and not to idle and non-responsible outsiders. The Dennison scheme is not like any previous scheme known to the writer. Doubtless its essential features will find their way into the organization of other companies. Its unfolding history, and the history of other similar corporations will be studied with deep interest by all persons who believe that radical improvement is possible in the organization of industry.